(20)

NO. 89-1279

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1989

Pacific Mutual Life Insurance Company,

Petitioner,

v.

Cleopatra Haslip, Cynthia Craig, Alma M. Calhoun and Eddie Halgrove,

Respondents.

On Writ of Certiorari To The Supreme Court of Alabama

BRIEF OF SOUTHEASTERN LEGAL FOUNDATION, INC. AS AMICUS CURIAE IN SUPPORT OF PETITIONER

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INTEREST OF AMICUS

The Southeastern Legal Foundation, Inc. ("Southeastern") submits its brief *amicus curiae* in this case. The parties have consented to the filing of this brief. Petitioner's consent letter has been filed with the Clerk of this Court. Respondents have issued a blanket consent for all parties wishing to file amicus briefs.

Southeastern is a non-profit corporation organized in 1976 for the purpose of advancing public interest viewpoints in adversarial proceedings involving signifi-

cant issues. Dedicated to economic and social progress through the equitable administration of law, Southeastern presents the views of its supporters who believe the rights of all persons should be properly protected and balanced in the courts. Towards that end, Southeastern has participated as *amicus curiae* in a number of cases before this Court, including *Common Cause v. Schmitt*, 455 U.S. 129 (1982); *Federal Energy Regulatory Commission v. Mississippi*, 456 U.S. 742 (1982); *South Florida Chapter of the AGC of America, Inc. v. Metropolitan Dade County, Florida*, 723 F.2d 846 (11th Cir. 1984), *cert. denied* 469 U.S. 871 (1984); *Aetna Life Insurance Co. v. Lavoie*, 475 U.S. 813 (1986); and *City of Richmond v. J.A. Croson Co.*, _____ U.S. _____, 109 S.Ct.706 (1989). Additionally, Southeastern has recently submitted *amicus curiae* briefs in *Astroline Communications Company Limited Partnership v. Shurberg Broadcasting of Hartford, Inc.*, Case No. 89-700, and *U.S. v. Eichman* and *U.S. v. Haggerty*, Case Nos. 89-1433, 89-1434, which are pending before this Court.

STATEMENT OF THE CASE

Southeastern adopts the statement of the case contained in the brief on behalf of Petitioner Pacific Mutual Life Insurance Company.

SUMMARY OF ARGUMENT

From an economic point of view, excessive punitive damages deter businesses from engaging in activities

beneficial to society. Excessive punitive damages stifle research and development of new products, and suppress innovative thinking and the application of novel ideas in service oriented businesses.

American business has learned to manage and quantify the economic risks of research, but cannot assess the risks of future legal costs due in large part to the uncertainty of punitive damages. The result is that many important products and innovative applications of new ideas are withdrawn from the public, sold in restricted markets, or never developed at all. Worse yet, such an environment stifles initial research in legally "high risk" areas from its inception. It is therefore not surprising that the United States is losing its perennial advantage of fostering innovative thinking and basic research, an advantage due in large part to this country's past commitment to free enterprise ideals and a legal environment that did not deter creative thought.

While *Amicus* contends that an agency relationship was not established, under the facts of this case, the decision of the Alabama Supreme Court could have an adverse impact on agency relationships in the business setting. Agency relationships will be jeopardized if juries require principals to be liable for punitive damages for the actions of their agents, even after the principals have performed satisfactory background checks and maintain adequate business supervision.

ARGUMENT

I. EXCESSIVE PUNITIVE DAMAGES OVERCOMPENSATE PLAINTIFFS AND DETER BUSINESSES ENGAGED IN USEFUL ACTIVITIES; THIS DETERRENCE

STIFLES RESEARCH AND DEVELOPMENT AND INNOVATIVE THINKING, AND NEEDLESSLY RESTRICTS THE AVAILABILITY OF IMPORTANT PRODUCTS TO U.S. CONSUMERS AND BUSINESSES, AND UNNECESSARILY REDUCES U.S. COMPETITIVENESS ABROAD.

Punitive damages are assessed in addition to compensatory damages to punish the defendant for the commission of an aggravated or outrageous act of misconduct and to deter him and others from such conduct in the future. *Restatement (Second) of Torts*, Section 908(1) (1977). However, from an economic point of view, excessive punitive damage awards inhibit conscientious businesses from engaging in activities beneficial to society. D. Ellis, *Fairness and Efficiency in the Law of Punitive Damages*, 56 S. Cal. L. Rev. 1, 47 (1982); D. Dobbs, *Ending Punishment in "Punitive" Damages: Deterrence-Measured Remedies*, 40 Ala. L. Rev. 831, 859 (1989).

If the potential liability of engaging in an activity outweighs the potential gain of the endeavor, a business will not pursue the activity even though the result would be an asset to a certain segment of our society, or to society in general. Similarly, even if the business incorrectly perceives the potential liability to be more than it actually is, the business will not pursue the activity. These attitudes are becoming prevalent among businessmen according to several commentators. R. Mahoney & S. Littlejohn, *Innovation on Trial: Punitive Damages Versus New Products*, 256 Science 1395 (1989).

A. MANY BUSINESSES DO NOT TRUST THE JUDICIAL SYSTEM TO FAIRLY ADJUDICATE PUNITIVE DAMAGE CLAIMS.

Today many businesses do not trust the judicial system to adjudicate punitive damage claims fairly and impartially. By analogy, in the late 1960's and 1970's, although innocent of negligent product design, manufacturers were still found liable under strict liability theories. Manufacturers who painstakingly considered every safety feature imaginable, enough to win any claim of negligent design, were shocked to learn that they might be liable under an unanticipated "new" legal device that made all their efforts for a safe design irrelevant. Just as the use of strict liability became commonplace in the 1970's, businesses today are afraid that excessive punitive damages will become commonplace in the 1990's. *See* R. Mahoney, at 1395.

Businesses assess risks. Businesses can even make the difficult assessment of whether the risk of scientific research today will later pay out in profits many years from now. But businesses today say that they are incapable of proper risk assessment due to the uncertainty created in the courts. R. Mahoney, at 1395. Adding to this fear is the fact that risk assessments made for products introduced in the 1960's were shattered with the use of strict liability in the 1970's. Businesses are afraid that history may be repeating itself in the form of punitive damages. R. Mahoney, at 1395-1397; *see also* E. McGuire, *The Impact of Product Liability*, Report No. 908 (The Conference Board 1988) at 8, 20 (Discussing the results of a 1988 Conference Board survey of chief executive officers from the nation's leading companies).

Although large punitive damage claims are rarely awarded, businesses are forced to bear the increased cost of

more claims and higher settlements. Even one large punitive damage award tends to bring out a multitude of claims from plaintiffs hoping to be the "lucky one". R. Willard and R. Willmore, *An Update on the Liability Crisis* (U. S. Dept. of Justice 1987) 47-51. This increases the number of suits filed, thus raising the cost of legal fees for potential defendants. Further, studies have shown that settlements where punitive damages claims are involved are much higher than without them. One study showed that settlements of claims where plaintiffs sought punitive damages were nearly 150% higher than similar settled disputes without punitive damages claims; another study showed that the prospect of punitive damages being awarded increased settlements by 60%. *See, Claim File Data Analysis: Technical Analysis of Study Results 86-87* (Insurance Services Office 1988) at 86-87.

Research has also shown that corporate defendants are more likely to be the target of punitive damages claims than individuals, and that juries also award more to plaintiffs when the defendant is an institution or organization as opposed to an individual. A. Chin and M. A. Peterson, *Deep Pockets, Empty Pockets: Who Wins in Cook County Jury Trials* (The RAND Corp. 1985) at 27.

Businesses have developed an overcautious attitude. Recent court decisions have fostered an environment where businesses cannot feel comfortable in their risk assessments when introducing new products or innovative business ideas. "Consulting engineers report that they systematically favor old products over new ones in their design specifications, fearing (quite correctly) that newer design options carry a greater risk of liability, whatever real decrease in risk they may actually represent." P. Huber, *Liability: The Legal Revolution and Its Consequences* 156 (1988).

Both businessmen and commentators realize that the standards for assessing punitive damages are tenuous at

best. Richard J. Mahoney, Chairman and CEO of Monsanto Company stated that: "[t]he punitive damages system makes it too easy for lawyers to mislead jurors, many of whom possess little scientific background but believe in the possibility of a risk-free society, to enrich plaintiffs and their attorneys with multimillion-dollar windfalls." R. Mahoney, at 1396. Mr. Mahoney's fears were expressed by noted legal commentator Richard Epstein over ten years ago. "[I]t is [easy] to slide over the gulf that lies between the willful and flagrant conduct suitable for a punitive damages award to the type of mistaken decision that supports at most a negligence cause of action." R. Epstein, *Modern Products Liability Law*, 1987 (1980). Without firm guidance governing the application of punitive damages, it is understandable that businesses have developed an overcautious attitude concerning their liability.

B. EXCESSIVE PUNITIVE DAMAGES LIMIT PRODUCT AVAILABILITY AND DEVELOPMENT

As a result of the overcautious attitude produced by the uncertain legal environment, many developed products are never introduced into the market place. For example, Monsanto has developed a safe, biodegradable substitute for asbestos, but potential expansion of liability laws has caused Monsanto to cancel the product just before commercialization. R. Mahoney, at 1397. The American Medical Association has determined that because of the legal environment, the development and use of potentially life-saving medical technologies is adversely affected. *See* American Medical Association,

"Impact of Product Liability on the Development of New Medical Technologies," *Proceedings House of Delegates* (137th Annual Meeting June 18-22, 1988) 88.

The same report notes that biomedical research is deteriorating and some companies involved in innovative research are delaying or foregoing product releases. *Id.* For example, Union Carbide has decided to cancel development of its suitcase-sized kidney dialysis unit as well as offering intravenous equipment. *See* W. Anderson, Remarks made at the Annual Meeting of the National Association of Casualty & Surety Executives, White Sulphur Spring, W. Va. (October 7, 1986).

Development of new vaccines for children may never occur as it has been estimated that 95% of the cost of developed childhood vaccines are to cover liability insurance. P. Huber, at 3, 155-161.

Only two U.S. companies are now conducting contraceptive research, an area where the U.S. was a dominant leader. E. B. Connell, *Technology Review*, Vol. 90, No. 19 (May-June 1987). Likewise, foreign manufacturers are hesitant to introduce their products in the U.S. because of the legal environment and potential for high punitive damages awards: these products include FDA approved medical products as well as products American businesses need to compete abroad. R. Mahoney, at 1397.

Some products may be introduced but only in limited areas to avoid potential liability in legally "high risk" applications. For instance, a chemical manufacturer refused to allow its product to be used in aircraft landing gear even though it is believed that the use of the product in landing gear would make them safer. P. Reuter, *The Economic Consequences of Expanded Corporate Liability: An Explanatory Study* (The RAND Corp. 1988) 25-27.

Researchers and those who make useful discoveries are finding it hard to find buyers to implement their ideas. For instance, the Lawrence Livermore Laboratory in California is finding it difficult to generate interest in its food irradiation invention for killing insects, larvae and parasites in fresh fruit and vegetables. *Does the Fear of Litigation Dampen the Drive to Innovate?* The New York Times, May 12, 1987, at 1.

In addition to paying higher prices for goods and services due to businesses passing on their own costs for legal expenses, consumers will pay even higher prices due to the lack of competition. In the 1960's there were eight U.S. manufacturers of whooping cough vaccine, by 1986 there were only two. P. Huber, at 156. Only two major American pharmaceutical companies, Merck and Lederle Laboratories, are investing heavily in vaccine research. *Business Struggling to Adapt as Insurance Crisis Spreads*, Wall Street Journal, January 21, 1986, at 20. It is inevitable that the availability of medical services will be reduced due to the unpredictability caused by punitive damages and society as a whole will be harmed.

C. EXORBITANT PUNITIVE DAMAGES STIFLE BASIC RESEARCH AND INNOVATIVE THOUGHT

Perhaps the most alarming "non-statistic" is the deterrent effect that uncontrolled punitive damages have on basic research. According to the National Academy of Sciences, "given the extremely high cost of vaccine-related injuries, many manufacturers may be unwilling to initiate or pursue the derivation or distribution of a vaccine to prevent AIDS." *See* American Medical

Association, at 86. One article quoted pharmaceutical industry representatives who gave the example of the bench chemist "who simply chooses not to pursue his curiosity about pregnancy-related drugs because he knows that the firm's senior management is unlikely to fund later and more costly stages of the development process for such a high-hazard product." P. Reuter, *The Economic Consequences of Expanded Corporate Liability: An Exploratory Study* (The RAND Corp. 1988) 25-27.

Burt Rutan, the designer and pilot of Voyager (the first airplane to fly non-stop around the world) stopped selling his construction plans for innovative airplanes in 1985 because he feared potential lawsuits that might ensue from crashes of home-built planes based on his designs. P. Huber, at 156. For similar reasons, a Virginia engineer whose son was crippled in a motorcycle accident had to abandon his business of designing better hand controls for cars used by the handicapped. Michael Brody, *When Products Turn Into Liabilities*, Fortune, March 3, 1986 at 60. In order for such innovative thinkers to share their ideas with the world they must risk all that they own, as insurance is generally cost prohibitive for such small businesses, if available at all.

Universities, fearful of liability concerns, are refusing to license patents to small companies fearful that anyone suing the company will also try for the university's deep pocket. *Does the Fear of Litigation Dampen the Drive to Innovate*, The New York Times, May 12,1987, p.1.

Companies that choose to pursue research in spite of the potential for high punitive damage awards will need to install more layers of management to further supervise product quality and access potential risks. The cost for the increased supervision will likely directly reduce

funds available for research. Further, the presence of these additional management layers and the protocols involved in decision making could encumber the otherwise free development process.

D. EXCESSIVE PUNITIVE DAMAGES WEAKEN U.S. COMPETITIVENESS ABROAD

The prospect of uncertain legal risk undoubtedly has effected U.S. competitiveness abroad. "More so than any other economy, the United States today depends critically on its ability to innovate, and to capture the benefits from innovation, for its economic prosperity." D. J. Teece, *The Competitive Challenge: Strategies for Industrial Innovation and Renewal*, 3 (1987). As mentioned previously the U.S. has lost its leadership role in the contraceptive area. Among other industries, the U.S. is also losing its dominant position in-aircraft production. In 1979 the domestic aircraft industry produced 18,000 planes, but in 1986 only 1500 were produced, with a corresponding decrease in employment of 70%. *Product Liability (Part 1): Hearings before the subcommittee on Commerce, Consumer Protection, and Competitiveness of the House Comm. on Energy and Commerce*, 100th Congress, 1st Sess. 550 (1987) (statement by Frederick B. Sontag, President, Unison Industries and Chairman, Product Liability Committee, General Aviation Manufacturers Association).

Punitive damages are basically unknown in civil law countries and rare in Great Britain and Canada. R. Mahoney, at 1396; B. Chapman and M. Trebilcock, *Punitive Damages Divergence in Search of a Rationale*, 40 Ala. L. Rev. 741, 745-758. If the legal environment

becomes too oppressive in the United States, it is not inconceivable that U.S. manufacturers will refuse to sell their products domestically. At Norplant, an implantive contraceptive that releases a hormone for five years, was developed by the New York Population Council; it is marketed in five countries but no American company has dared to market it at home. P. Huber at 155. These manufacturers may move their operations abroad in order to get closer to their markets and get favorable tax and tariff treatment resulting in lost jobs for Americans.

E. EXCESSIVE PUNITIVE DAMAGES ADVERSELY EFFECT AGENCY RELATIONSHIPS WHICH ARE IMPORTANT TO THE PRESENT AND FUTURE SUCCESS OF AMERICAN BUSINESSES.

The effects of potentially unreasonable punitive damages awards are somewhat easy to comprehend in product development situations; new products will not be developed. However, the United States, while still a manufacturing leader, is becoming more service oriented. In order to remain a leader in the service sector, American businesses must become even more innovative in how they use their skilled personnel.

One very important way for American businesses to remain competitive in the service industry sector is to develop their use of agency relationships. Courts need to clearly define when and to what degree principals will be liable for acts of their agents, particularly in the area of potential punitive damages, so that businesses can make knowledgeable risk assessments of whether to use agents. Economics often dictates that, if a business is to provide a service in a particular area it must use an

agent as the costs of an employee would not be cost efficient. If businesses perceive that there is a possibility that they may be liable for punitive damages from the acts of the agent, the service will not be provided.

Agency relationships are important to American businesses and competitiveness for at least four reasons. First, many businesses are ideally suited to principal-agent relationships as opposed to an employer-employee relationship, such as the real estate industry and the insurance industry. Second, small businesses, like those "garage businesses" started by Ross Perot and Walt Disney, require agents to sell their products and supply services, as small businesses cannot hire full time specialists. Third, with a projected shortage of skilled workers, America will need to lure homemakers back into the work place; many returning homemakers will probably want to work as agents in their specialized field as this will allow for shorter or more flexible hours than full-time work. Fourth, in order to remain a world competitor with a shortage of skilled labor, skilled workers will have to share their expertise with several businesses, agency relationships will be invaluable for many of these situations. Further, many talented people do not want to work as employees as they enjoy the flexibility and tax benefits they receive by being self employed agents.

As agency relationships generally allow the agent more autonomy than an employee, courts must realize, in determining if punitive damages are justified, that a principal has much less supervisory control than an employer. Secondly, as agency relationships will become more common, courts should not hold principals vicariously liable in punitive damages for the acts of their agents if the principals made reasonable background checks of the agent and otherwise exercised responsible standards of care.

II. PUNITIVE DAMAGE AWARDS OF MORE THAN DOUBLE THE COMPENSATORY AWARD ARE JUSTIFIED IN ONLY FOUR CIRCUMSTANCES.

While there are circumstances where punitive damages may be appropriate, there are only four situations where punitive damages multiples of compensatory damages above two are justified.

First, where the actual damages are low as compared to the legal cost of bringing the action and large multiples are required to encourage "private attorneys general" type actions. *See Roginsky v. Richardson-Merrell*, 378 F.2d 832, 841 (2d Cir. 1967) (J. Friendly writing for the majority). This situation is easily shown by the plaintiff's attorney's actual time and expenses.

Second, where the defendant may conceal the injury from a large number of victims, large multiples are required to destroy the defendant's economic incentive to maintain its behavior and pay the damages. For example in *Boise Dodge v. Clark*, 92 Idaho 902, 453 P.2d 55 (1969), the defendant car dealership rolled back odometers on the demonstrator cars it sold representing them as new. The court justified a punitive damage award of approximately 35 times the compensatory damages as it estimated that few purchasers would discover the dealership's egregious behavior. The court held that the punitive damage multiple would have to be sufficient to destroy the defendant's economic incentive to maintain the practice. It is also important to note that

the compensatory award was only $350.

Thirdly, large multiples are also justified where the defendant actually considered that its actions would still be cost efficient even if it had to pay punitive damages of a small multiple. *See Grenshaw v. Ford Motor Co.*, 119 Cal. App. 3d 757, 174 Cal. Rptr. 348 (1981).

Lastly, large multiples are also justified where the defendant has been found "guilty" of similar intentional or reckless behavior and punitive damages were assessed; the defendant had notice of its "criminal" activity by "conviction" of a similar offense and still committed the "crime".

The burden should be on the plaintiff when requesting punitive damages to show that one of the four situations above exists, thus entitling the plaintiff to a punitive damages multiple greater than two. The plaintiff should have little difficulty making a showing sufficient to shift the burden to the defendant if any of these situations indeed exist.

It is important to note that many groups and commentators even restrict the multiple to two where there are large compensatory awards. *E.g.*, American College of Trial Lawyers, *Report on Punitive Damages* 15 (1989).

Plaintiff's lawyers may argue that there is a fifth situation where large punitive damages multiples are justified; that being where the defendant is very wealthy. The standard argument is that large punitive damages are required to "get their attention" where smaller awards are satisfactory to gain the attention of less wealthy defendants. Owen, *Problems in Assessing Punitive Damages Against Manufacturers of Defective Products*, 49 U. Chi. L. Rev. 1, 45-46 (1982). If this reasoning is correct, all punitive damages assessed

against large corporations would have to be at least six or seven figures. *Id.* This reasoning tends to equate large corporations to extremely wealthy individuals. A corporation, however, cannot be viewed simply as an entity; it is an assemblage of individuals and stockholders. *See Id.* at 15.

It is important to note that there is no evidence that punitive damages actually do deter businesses, especially corporations, from unethical behavior. E. D. Elliott, *Why Punitive Damages Don't Deter Corporate Misconduct Effectively*, 40 Ala. L. Rev. 1053, 1062 (1989).

Punitive damages of any amount bring media attention; and extremely large awards give rise to a great deal of media attention. Adverse media attention often causes damage to the business's reputation, resulting in lost profits. *See Roginsky v. Richardson-Merrell*, 378 F.2d 832, 841 (1967). Far worse than adverse news coverage is the closing of a business. As Judge Friendly noted, "a sufficiently egregious error as to one product can end the business life of a concern that has wrought much good in the past and might otherwise have continued to do so in the future . . ." *Id.* The loss of jobs, increased insurance premiums, and more expensive products are all costs borne by the general public. While outrageous behavior must be checked, it is the average person or consumer who ultimately pays for every award issued in a court of law.

IV. CONCLUSION

This Court should consider the extrajudicial impact of exorbitant punitive damages on American businesses *and* the United States economy. Definite standards must be established for courts to follow when determining the amount of punitive damages to award. Accordingly, Amicus respectfully requests that the decision of the Alabama Supreme Court be reversed.

Respectfully submitted,

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